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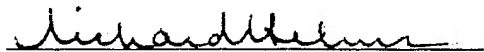
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NUMBER 11-5-67

Soviet Economic Problems and Prospects

Submitted by



DIRECTOR OF CENTRAL INTELLIGENCE

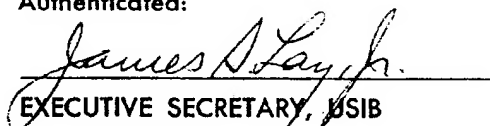
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CONTENTS

	Page
SUMMARY	1
DISCUSSION	3
I. GENERAL PERFORMANCE	3
II. PROBLEMS AND PROSPECTS	5
Economic Reform	5
Industry	6
Agriculture	7
Defense and Space Spending	7
Living Standards	8
Plans and Prospects	10
III. FOREIGN ECONOMIC RELATIONS	12
Trade with the Industrial West	12
Economic Relations with Eastern Europe	13
Aid and Trade with the Third World	14
IV. POLITICAL IMPLICATIONS	16

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SOVIET ECONOMIC PROBLEMS AND PROSPECTS

SUMMARY

A. After some years of slowdown in its rate of growth, the Soviet economy had a good year in 1966. Gross national product (GNP) grew an impressive 8 percent. Though much of this gain was due to favorable weather and a record harvest, the leadership can take credit for some of the improvement. But last year's performance is not necessarily a harbinger of a durable upward trend. Many serious problems remain in an economy which uses resources inefficiently and is still backward in many sectors.

B. The leadership has been trying to effect a return to the high rates of growth which prevailed in the 1950's by a reform of administrative structures, planning procedures, and incentive programs. The authority of enterprise managers has been strengthened, and interest charges on the use of capital and new success indicators (including sales and profitability) have been introduced. While such measures represent improvements, the reform program as a whole is an essentially timid response to a large problem; the leadership is clearly concerned that a more thoroughgoing reform might jeopardize its political controls.

C. The share of GNP devoted to defense and space spending has declined in recent years, but the burden on the economy has not. The resource demands arising from research and development and the production of advanced weapons systems have used high quality manpower and top-grade materials faster than the growth of the economy can comfortably support. We foresee no real easing of these strains. Moreover, total military and space spending will probably increase through at least 1970 at about the same rate as the rise in total output.

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D. Partly as a consequence, living standards are likely to rise only very gradually. Much of the planned growth in per capita real income is dependent on boosts in productivity which may not materialize. Further, as in the past, consumer programs are likely to be among the first to suffer if plans go awry in higher priority sectors.

E. The goals of the current Five-Year Plan (1966-1970) will require average annual growth rates comparable to those of the 1950's-- 8 to 8.5 percent in industrial production, and nearly 5 percent in agricultural output. We estimate that industrial output will be somewhat short of its target, and that the annual growth of agricultural output will fall somewhere between 3 and 5 percent (assuming normal weather). Overall growth (GNP) may achieve an annual rate ranging from 4 to 6 percent.

F. The Soviets view trade with the industrial West as an especially valuable means to help overcome backwardness in certain sectors of the economy. They are likely to continue their drive for an expansion of this trade, which has more than doubled over the past 10 years. Trade with the West will almost certainly not climb at the very rapid pace characteristic of the early 1960's, though it will probably increase at about 6 percent per annum.

G. It seems doubtful that economic issues will soon produce another major unsettling of the political scene. The current leadership appears to recognize that the USSR's economic problems are tremendously complex and not susceptible to quick and easy solutions. Should the round of reform and adjustment which has been going on for the last two years or so ultimately fail, however, a renewal of leadership struggle over economic policy is entirely possible.

H. The condition of the economy does not at present carry any very marked implications for Soviet foreign policy; ample resources will continue to be available for support of a large arms effort, foreign aid, and other instruments of external policy. The Soviet leaders appear, however, to be preoccupied with their economic problems and in a general sense wish to avoid involvements abroad which would bring new economic burdens.

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DISCUSSION

1. After some years of slowdown in its rate of growth, the Soviet economy had a good year in 1966. For several years the Soviet leaders have been struggling, sometimes with each other, to devise ways of overcoming the slowdown, since their plans both at home and abroad depend on a continuing high rate of advance. In part, their problems are those of success. The economy has grown so large and complex that the traditional command methods of planning and direction are no longer adequate. The improved performance of 1966 probably owes something to measures the leadership has taken, but it owes more to record crops brought by unusually favorable weather. The question for the future is whether the leadership will be able to devise policies which would return the economy to a high rate of advance on a sustained basis.

I. GENERAL PERFORMANCE¹

2. During the first 5 years of this decade, the average annual growth rate of the Soviet economy fell to about 4.5 percent, down from about 6.5 percent in the last half of the 1950's. This significant decline can be attributed primarily to the sharp drop in the rate of growth of productivity. In the 1950's, the growth in the productivity of labor and capital (plant and equipment) averaged more than 2.5 percent each year, and this alone accounted for about two-fifths of the growth in total output. In the first half of the 1960's, however, gains in total output were attributable almost entirely to the growth of labor and capital inputs, i.e., of actual manhours, plant, and equipment. (See Figure 1.)

3. The precipitous decline in growth of productivity was the consequence of several important developments: (a) a marked slowdown in the pace at which new and more modern plant and equipment was introduced; (b) continuing delays and difficulties in the utilization of new equipment—faulty design and assembly work, shortages of educated and trained operating personnel, organizational shortcomings; (c) the continuing drain of highly skilled men and top grade materials by the defense effort; (d) the increased costs of technological modernization and innovation as the economy advanced; and (e)

¹ Although we accept most of the Soviets' official commodity statistics, we do not accept their aggregate measures of growth (e.g., for national income and industrial output), or their statistics on agricultural output, which we believe are substantially overstated. The aggregates and the agricultural figures used in this estimate were calculated by CIA and accepted by the intelligence community.

Rates of growth and other statistical comparisons in the estimate have been carried out numerically to the degree required to make valid comparisons. The presentation of the data to the first decimal point, however, does not necessarily reflect a comparable degree of accuracy in either the absolute level of a given value or in the absolute difference between two values.

The base year used in deriving average annual rates of growth is the year preceding the given year or period.

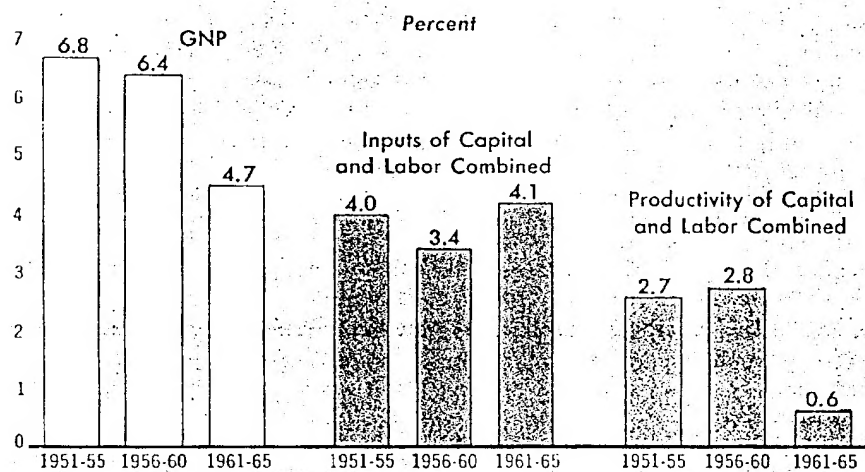
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Figure 1

USSR: Average Annual Rates of Growth of GNP, Inputs of Capital and Labor, and Productivity of Capital and Labor, 1951-65



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the growing confusion, inefficiency, and unwieldiness of industrial and agricultural administrative systems, combined with continued shortcomings in incentive systems and in the methods of evaluating economic progress.

4. Preliminary calculations indicate that the growth of productivity increased sharply in 1966, exceeding somewhat the high rate characteristic of the 1950's and markedly advancing over that of the first half of this decade. This was reflected in an impressive gain of almost 8 percent in industrial production and a record output in agriculture. The result was a rise in GNP of nearly 8 percent compared to less than 5.5 percent in 1965 (and an estimated 5.5 percent in the US in 1966). Much of this gain was undoubtedly due simply to fortunate circumstances—good weather and an unusually good harvest. It does not necessarily follow that the 1966 performance is a harbinger of a durable upward trend in the economy; many serious problems remain.

II. PROBLEMS AND PROSPECTS

Economic Reform

5. Serious dissatisfaction with the performance of the Soviet economic system led in 1965 to an announcement by Premier Kosygin of a comprehensive program of reform. Over a period of several years, the administrative structure of the economy is to be revamped at both the national and enterprise levels, the system of planning is to be modernized, and the methods of gauging success and providing incentives are to be recast.

6. Within this broad framework of reform, several specific measures are being put into effect: (a) the old Khrushchevian system of management through regional economic councils (sovnarkhozy) has been abolished and replaced by a central structure consisting of 23 industrial ministries and a powerful planning commission (Gosplan); (b) the authority of enterprise managers over the use of their labor and working capital has been strengthened, and some can now develop limited contractual relationships with customers; (c) the number of centrally determined plan assignments and the detailed specifications accompanying them have been substantially reduced; (d) the old success indicators, gross value of output and unit costs—which encouraged managers to stress sheer quantity at the expense of quality and assortment—have been superseded by more meaningful indicators, including sales and profitability (return on fixed plus working capital); (e) a new interest charge of 3 to 6 percent on the use of capital has been introduced; and (f) prices, particularly industrial wholesale prices, are being subjected to review and are scheduled to be brought into line with average costs of production, which, for the first time, are to reflect charges for the use of capital.

7. The Soviet press has devoted considerable attention to the progress of the economic reform, reporting both the successes and problems of implementation. Enterprises which now function under the new system (some 2,500, accounting for about 20 percent of total industrial output) are said to have scored gains in sales, profits, and labor productivity considerably greater than those

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for industry as a whole. (Most of these enterprises, however, performed better than industry as a whole even before their transfer.) On the other hand, problems publicly discussed have included bureaucratic footdragging and meddling, the inefficiency of the banking system, the nonfulfillment of contracts by suppliers and customers, and inability to spend accumulated funds for capital improvements because of a lack of plans and shortages of manpower and materials. On the whole, the Soviet leaders have appeared to be satisfied with the initial results of the reform, though they remain committed to a cautious and piecemeal introduction of many of its features.

8. The economic reform contains some measures which may represent meaningful improvements over past practices, and clearly some progress is being made in its implementation. But the new program is less liberal and less ambitious than some now underway in Eastern Europe and is, in fact, an essentially timid response to a large problem. The Soviet leaders are clearly concerned about economic dislocations resulting from reform and, more important, the possible loss of political controls. Although a faint but audible theme of the reform is market socialism—interest, profits, a touch of the market mechanism—the new system remains tightly circumscribed by the old. Indeed, the principal attributes of a command economy—central direction and planning of production and centrally determined price structures—remain, and are intended to remain, fundamentally unaltered.

9. In the long run, as the current reform proves to be inadequate, as gains in efficiency turn out to be marginal or temporary, dissatisfaction (already voiced by some academic economists) will increase. A new round of reform proposals would then probably become the subject of controversy within the leadership.

Industry

10. The 6.4 percent average annual rate of growth of industrial output during the first half of this decade was considerably lower than the rate maintained in the 1950's (about 9.3 percent). A pronounced decline in the growth of productivity in industry seems to have been primarily responsible. But Soviet industrial production rose by an estimated 7.8 percent last year. Productivity was up, perhaps largely as the result of the assimilation of new capacity at a faster pace and more efficient manner than has generally been the case in the past.

11. The current Five-Year Plan (1966-1970) calls for about a 50 percent rise in both industrial output and investment. The investment target for industry is about an 8 percent rise per year, and the planned annual increase in employment is less than 2 percent. Priorities are assigned to the development of the chemical, metallurgical, machinery, oil and gas, and electric power industries. The output of many consumer durables is to be boosted substantially; the production of automobiles, for example, is to be nearly quadrupled—from 201,000 in 1965 to 750,000 in 1970. We believe that industrial productivity and output will grow at faster rates than in the first half of the 1960's, but will fall somewhat short of plan goals.

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Agriculture

12. Agricultural production in the USSR in the years 1956-1960 averaged some 36 percent above the level of 1951-1955. But during the first half of this decade, a period in which both incomes and expectations grew appreciably, the average annual output was only about 11 percent above that of the preceding five-year period and, on a per capita basis, was only about 2.5 percent higher. In 1963-1965, the average annual net imports of grain equalled 11 percent of domestic output, as against net exports of an average 7 percent in 1960-1962. Increases in crop and livestock production in 1966 have, of course, at least temporarily reversed the trend toward agricultural stagnation. Overall net output grew by an estimated 10 percent and both the grain harvest and the output of meat and milk reached record highs. (Grain production totaled an estimated 135-140 million metric tons, up from 100 million in 1965 and 120 million in 1964.)

13. The current Five-Year Plan calls for agriculture to receive twice the investment it did in 1961-1965 and a growing share of total investment: 25 percent in 1970 vs. 18 percent in 1965 (compared to 6 percent in the US in 1966). Deliveries of farm machinery are scheduled to increase at a faster rate, fertilizer output is to double, the area of reclaimed land is to expand by a third, and farmers are to be provided with additional financial incentives. This massive program is somewhat behind schedule; both investment growth and the output of farm machinery are running behind rates necessary to meet the 1970 goals. Nevertheless, considerable progress has been made in most areas of the program; good weather in 1966 was no doubt primarily responsible for the bumper crops, but the greater availability of fertilizers and the introduction of a variety of incentives for the farmer probably contributed in an important way to the rise in output. Assuming normal weather and no slackening in the determination of the regime, we estimate that agricultural production will increase 3 to 5 percent annually during the period 1966-1970; close to a 5 percent average annual increase is required to meet plan targets.

Defense and Space Spending

14. Following several years of relatively modest increases, total Soviet military and space expenditures rose sharply in 1966 and will probably show a further increase to more than 20 billion rubles in 1967, some 16 percent higher than the figure in 1965. Though the share of GNP devoted to defense and space spending has actually declined in recent years—from about 16 percent in 1950 to less than 10 percent—the burden on the economy has not really been eased. There has been a significant shift in the composition of military expenditures, away from emphasis on the relatively simple wants of the general purpose forces and toward the complex requirements of research and development (R&D) and the strategic forces. Thus expenditures for military R&D and space rose from only 4 percent of total military and space spending in 1950 to about 27 percent in 1966, and the share devoted to strategic offense and strategic defense increased from about 6 percent each to some 13 percent each during the same period. The volume of resources devoted to general

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purpose forces has remained roughly constant for the past six years, although the share of total expenditures given to these forces has declined from about 35 percent in 1961 to an estimated 28 percent in 1967. (See Figure 2.)

15. The military has been preempting high quality manpower and top-grade machinery and materials at a faster rate than the general growth of the economy can comfortably support. The resources needed by advanced military and space programs are also those most wanted by the civilian economy. Soviet industry and agriculture, for example, are in urgent need of R&D programs, but military and space requirements draw off the best scientific manpower and the bulk of the funds allocated for such purposes. Similarly, civilian industry is in great need of modern, technologically advanced production equipment, but the machine building industry, which is responsible for satisfying such needs, also bears the brunt of the production of advanced weapons systems. The sagging rates of growth of output, investment, and productivity in industry as a whole—only partly restored in 1966—can in part be attributed to the impact of military and space priorities.

16. Military expenditures through 1968 and 1969 are already fairly well determined by programs in progress. Expenditures will continue to reflect the rapid pace and large number of advanced programs being pursued simultaneously and the maintenance of a strong R&D effort. Trends after 1969 will reflect in part decisions not yet made. These will reflect the Soviets' appraisal of US policies, their view of the international climate as a whole, and in particular any US military involvements at that time; and to some extent, their evaluation of the impact of military spending on the remainder of the economy. Our best judgment at this time is that Soviet military and space spending (19 billion rubles in 1966) will grow to some 23 billion rubles in 1970. In general, these increases in military expenditures will be more or less in line with the rise in total Soviet output, but will continue to take resources badly needed in other sectors of the economy.

Living Standards

17. The standard of living of the Soviet people as a whole has been growing at a slow pace since 1960. (See Figure 3.) Per capita consumption of goods and services nearly doubled between 1950 and 1966 but almost two-thirds of that increase occurred before 1958. Consumer-oriented investment (i.e., investment in agriculture, housing, consumer goods industries, and services) grew only some 5.5 percent annually in the years 1961-1965; it grew about 6.5 percent in 1966. Gains were registered in 1966, especially in the consumption of both soft and durable goods, but the completion of new housing was up by only 1 percent (compared to a plan goal of 12.5 percent). A development in income distribution which may have important long-term social and economic effects is the marked improvement which is occurring in earnings of the rural population. The regime believes that removal of the vast disparity in living standards between city and country will help to promote productivity in agriculture, on which so much in current economic plans depends.

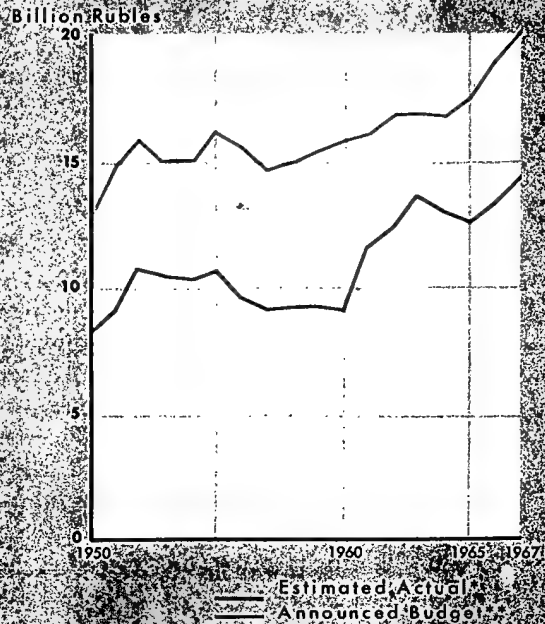
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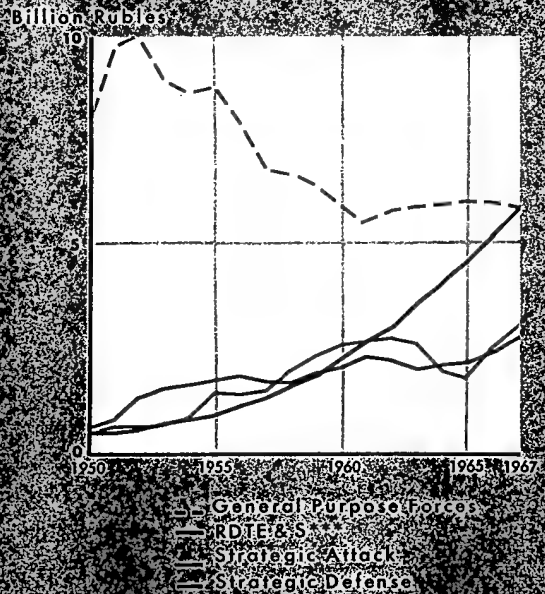
SOVIET DEFENSE EXPENDITURES, 1950-1967

Figure 2

Announced Budget vs. Actual Outlays



Major Military Missions



Expressed in 1955 Prices
Expressed in Current Prices
Research, Development, Test, Evaluation, and Space

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18. Living standards are likely to improve only gradually over the next several years. The leaders have promised the consumer a better deal, and have made some moves in this direction, but they have also bluntly stated that gains in consumer welfare scheduled in the Five-Year Plan are contingent on a resumption of high growth rates in productivity. Much of the planned, fairly substantial growth in per capita real income is scheduled to come from increases in bonus payments and is thus also dependent on boosts in productivity. Moreover, as in the past, consumer programs are likely to be among the first to suffer from short-falls elsewhere in the economy.

Plans and Prospects

19. The draft directives of the Five-Year Plan for 1966-1970 show that the present leaders have set their sights on regaining the economic momentum of the 1950's. The current Five-Year Plan has not been formally approved and may yet be extensively revised, but, as initially outlined, calls for or implies average annual growth rates comparable to those of the 1950's—6 percent in GNP, 8 to 8.5 percent in industrial production, and nearly 5 percent in agricultural output. These goals, while scaling down those for 1970 first put forward by Khrushchev in 1961, are nonetheless ambitious and—since the planned rates of increase in investment and in employment are relatively modest—will require a rapid resurgence in the growth of productivity; they jumped from the average annual rate of some 0.5 percent in the first half of the 1960's to nearly 2 percent in the last half.

20. In general, the outlook for the progress of the Soviet economy as a whole will depend on how successful the Soviets are in modernizing both their means (their work force, their plant and equipment, and the efficiency of their investment) and their methods (their allocation of priorities, structuring of management, and provision of incentives). As indicated, there are as yet few signs that the Soviet economic system is about to be transformed into an efficient, flexible, and responsive instrument. Moreover, some of the elements responsible for the rapid growth rate in the 1950's can no longer provide as much stimulus to growth at the present stage of the economy's development.

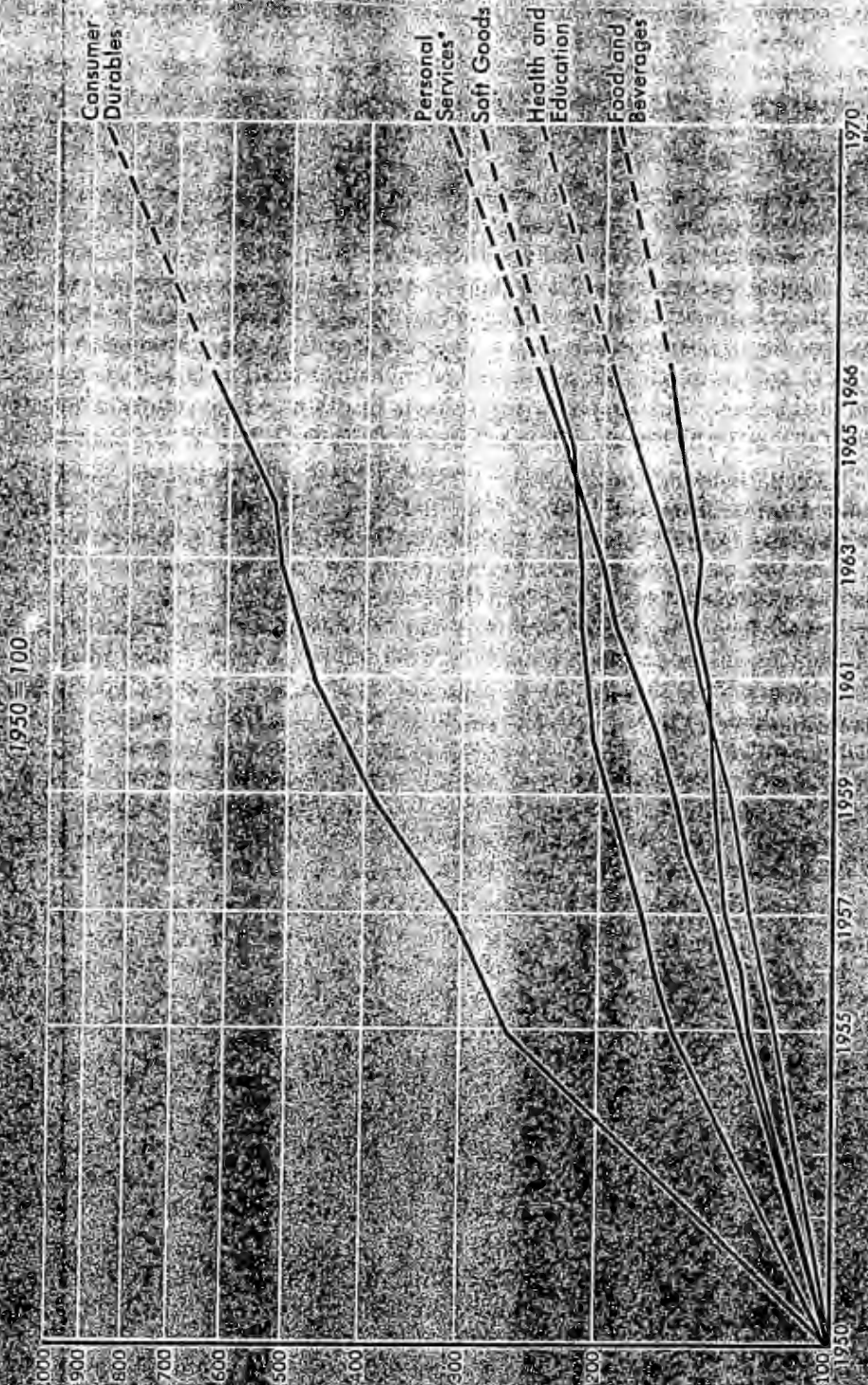
21. In those areas, generally the basic industries, where Soviet technology has been approaching the more advanced standards—and these areas account for much of manufactured output—it is no longer possible (as it was in the 1950's) to greatly increase output simply through the introduction of Western technology. Moreover, it is no longer possible to effect rapid improvement in the average age of capital stock and in the skills of the working force. Finally, in the years ahead, the USSR will find it difficult to maintain the rate of growth of total inputs to the economy (about 5 percent) since 1962. The pattern of growth of these inputs suggests, in fact, a rise on the order of 4 percent per year through 1970. Productivity, on the other hand, should improve over the early 1960's rate; a range of from more than 0.5 percent to 1.5 percent annually appears reasonable. Together, this productivity rate and the postu-

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Figure 3

USSR: Indexes of Growth in Major Components of Per Capita Consumption 1950-66 and 1966-70 Plan



*Household expenditures on rent, household operations, personal care, recreation, transportation, and communication.

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lated growth of inputs would permit an average yearly rise in GNP of from 4 to 6 percent.

III. FOREIGN ECONOMIC RELATIONS

Trade with the Industrial West

22. One partial answer the Soviet leaders have seen to the economic problems with which they have been coping in recent years lies in the development of their external trade, especially with the industrial West. The economic and technological backwardness of certain sectors of the economy results in part from its relative isolation from the more dynamic Western economies. The push the Soviets have tried to give to their trade with Western Europe in recent years, as well as to scientific and technical exchanges of all sorts, reflects recognition of this fact. This emphasis seems likely to continue as pressures mount for modernizing the unevenly developed Soviet economy.

23. Trade between the industrial West and the Soviet Union has more than doubled over the past 10 years. This development reflects not only a Soviet interest but also more generous credit terms provided by West European states as their interest in this market grew, partly for political reasons. In 1966, this trade amounted to about \$3.5 billion, about 20 percent of the \$16.8 billion total of Soviet foreign trade turnover. The USSR's hard currency deficit, some \$600 million in 1964, declined to about \$100 million in 1966. Sales of gold to offset these deficits dropped by comparable amounts, from \$520 million in 1964 to \$35 million in 1966. With the improvement in the USSR's balance of payments position, orders for Western machinery were greatly increased in 1966; these orders, which had fallen off sharply in 1964 and 1965, reached a record high of about \$800 million, nearly half of which was involved in the purchase of an automobile plant from Italy's Fiat. Payments on most of these orders will not begin for a number of years.

24. The US's share of Soviet trade with the industrial West is small; it amounted to some \$90 million in 1966, 0.5 percent of total Soviet foreign trade turnover and 0.2 percent of US trade. The USSR would probably like to see trade with the US increase, particularly if there were some relaxation in US embargoes on such strategically useful items as computers, advanced machine tools, and microelectronics. But most Soviet raw materials exports are not very attractive to US importers. Moreover, much of the machinery and equipment the Soviets are interested in is normally available from Western Europe and Japan at lower costs and more favorable terms than from the US. There thus seems to be little likelihood of any significant increase in US-Soviet trade.

25. Lack of suitable export goods will also continue to limit the growth of Soviet trade elsewhere within the industrial West. The West European market for Soviet coal, oil, cotton, and timber products is limited, as are world markets for Soviet ores and metals. Soviet manufactured goods—often badly made and poorly packaged—cannot compete with domestic manufacturers in Western

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Europe. Even Soviet agricultural products—should a succession of good crop years make the USSR a net exporter of food—would encounter protectionist barriers in Western Europe. Accordingly, Soviet trade with the industrial West will almost certainly not climb at the very rapid pace characteristic of the early 1960's, though it will probably increase at about 6 percent per annum. Given their present trade policies, and assuming no new reverses in grain production, the Soviets should be able to keep their hard currency deficit within manageable proportions over the next few years. In this case, their gold reserves—which sank to an estimated \$1.1 billion in 1965—would gradually rise.

Economic Relations with Eastern Europe

26. Although the absolute value of East European trade with the industrial West has increased greatly over the past 10 years (from \$1.9 billion in 1955 to \$4.8 billion in 1965), it has not done so at the expense of the Soviet Union, whose share of East European foreign trade has remained relatively stable. In 1966 Soviet trade with Eastern Europe amounted to \$9.2 billion, about 55 percent of total Soviet foreign trade turnover. Moscow's attitude toward the expansion of Eastern European trade with the West has been equivocal; the Soviet leadership has seen benefits in expanded trade and has done little to discourage it. But the dangers of political entanglement and economic imbalance within CEMA have also been apparent to Soviet leaders, and they have cautioned their allies not to go too far too fast.

27. Under Brezhnev and Kosygin, the Soviet Government has itself stimulated Eastern European interest in trade with the West by harder bargaining with its Eastern European partners. Moscow has come to realize that the rising cost of extracting and transporting many of the raw materials it has traditionally exchanged for East European manufactured goods has outstripped the cost of producing such goods in the Soviet Union. One consequence of this realization has been Soviet insistence on new pricing standards in Soviet-East European commodity trade, substituting prices based on high Soviet production and transportation costs for the system of world market prices used earlier. They have also sought Eastern European investment funds for the expansion of Soviet raw materials industries. The net effect of this new approach, if it comes into force, will probably be to make trade with non-Bloc partners still more attractive to the East Europeans than it now is, particularly in the areas of commodities and raw materials imports.

28. Nevertheless, in thus pursuing its own interests, the USSR runs no serious risk of losing its predominant economic position in Eastern Europe. The price concessions demanded by the Soviet Government are chiefly at the expense of Czechoslovakia and East Germany. Three-quarters of Soviet net exports of raw materials and semimanufactures to Eastern Europe go to these two countries. They are so dependent economically on the USSR that they have only limited leverage in resisting Soviet terms. The other four countries are not greatly affected by the new Soviet price demands; Bulgaria and Rumania, in fact, support them because their own trade would benefit. Moreover, the USSR has

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treated Bulgaria, Hungary, and Poland quite generously in the current trade agreement, in part surely to discourage them from following in the footsteps of Rumania.

29. The Soviet leadership appears to recognize that the trend toward looser economic and political ties within the Soviet Bloc will not be reversed. It hopes, however, to be able to slow the process and to set limits to it. The Soviets also recognize that an extensive development of Eastern Europe's relations with the West might stimulate more independence in the policies of these states than Moscow wants to see. They are already concerned, for example, by Rumania's growing trade and political ties in Western Europe, and the assertiveness toward Moscow which has accompanied them. On balance, however, we do not think the Soviets will find some further growth of Eastern Europe's trade with the West fundamentally incompatible with their own long-term interests, though they will remain concerned to preserve their own political and economic dominance in the area.

Aid and Trade with the Third World

30. Since 1954, the USSR has extended about \$6 billion in economic aid to some 35 countries of the underdeveloped world. In the same period, Soviet military aid extensions have totaled an additional \$4.3 billion. (See Figure 4.) While most of the military aid extensions have been drawn (about \$3.5 billion), only about one-third of economic aid extensions had been drawn by the close of 1966 (\$2.2 billion), and the net costs to the USSR are being steadily reduced by debtor repayments (about \$500 million has been scheduled for repayment so far). Much of this cost, however, may never be repaid—for example, by Indonesia, the UAR, and Ghana.

31. Brezhnev and Kosygin have maintained the essential features of the foreign economic assistance program pursued under Khrushchev. Extensions of new aid reached their highest annual total (more than \$1 billion) in 1964 under Khrushchev, but did not decline substantially in 1965 and 1966 when a two-year total of some \$1.7 billion was committed. The new leaders did, however, make some changes in their approach to the program. Specifically, they began to handle foreign assistance in a more deliberate fashion, abandoning the practice of extending large umbrella type credits before specific projects were negotiated. They also began to take advantage of a more receptive attitude toward Soviet aid in certain countries peripheral to the USSR (Turkey, Iran, and Pakistan), without, however, neglecting interests in such other favored recipients as the UAR and India.

32. In point of fact, the Soviet aid program represents no significant burden on the Soviet economy. From time to time, specific industries (e.g., the heavy construction equipment industry) in the USSR may feel the pressure of foreign aid deliveries, but at no time have the costs of these deliveries amounted to more than 0.1 percent of the Soviet GNP, and a more typical annual figure would halve that. Extensions of aid in the next few years will probably

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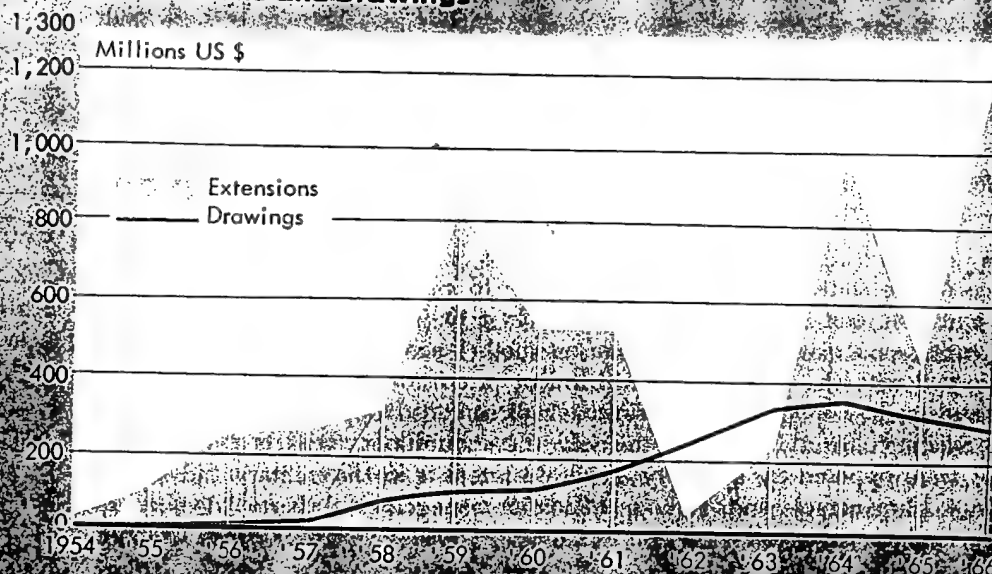
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Figure 4

Soviet Economic Aid to Less-Developed Areas of the Free World 1954-66

Annual Extensions and Drawings



Accumulated Extensions and Drawings

Area or Country	Extensions	Drawings
AFRICA	882	218
ASIA	2,811	1,316
Afghanistan	592	444
India	1,612	694
Indonesia	331	81
Pakistan	178	39
Other	198	58
LATIN AMERICA	147	31
MIDDLE EAST	2,149	616
Iran	330	111
Iraq	190	121
Syria	234	55
Turkey	208	8
UAR	1,011	380
Other	176	41
TOTAL	5,989	2,181

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follow past patterns, fluctuating from year to year with political circumstances and the demands of certain recipients. Drawings on aid are likely to rise from the \$350 million average of recent years to about \$400-\$450 million in 1970; the schedule of repayments rises from about \$115 million in 1965 and \$150 million in 1966 and is expected to almost double in the next 5 years. At the same time, the Soviet aid program has stimulated Soviet trade with aid recipients. This now accounts for nearly 11 percent of all Soviet foreign trade, and it will probably continue to increase at a rate of about 10 percent a year over the next few years.

IV. POLITICAL IMPLICATIONS

33. All Soviet leaders are inclined to look on the USSR's economy in terms of its political assets and liabilities, its strengths and weaknesses as the ultimate source of the state's power, and its capacity to sustain high national purpose and ambition. But such questions as how best to insure the economy's vigor, how much emphasis to attach to one or another economic program, and how to proceed with the allocation of investment priorities have long been abrasive issues in leadership politics. Khrushchev often faced opposition born in part of conflicting attitudes toward precisely these questions. His economic programs were opposed by a variety of vested interests in the military and heavy industry bureaucracy and among economic managers and party ideologues, not to mention among his own immediate colleagues. This opposition figured strongly in the coup that brought his downfall.

34. After Khrushchev's fall in 1964 there appeared to be a consensus within the top leadership on economic policy, at least on the point that no quick and dramatic solutions to the problems that had arisen were possible. This has apparently reduced controversy and indicates a tendency to make bureaucratic compromises which sidestep contentious decisions. Thus the leaders appear willing to try to appease the appetites of the military and the steelmakers, but so far they have been unable to agree even on the final version of the Five-Year Plan, and have dodged a number of painful decisions simply by assigning high priorities to a broad variety of competing tasks—strengthening national defense, developing heavy industry, raising agricultural production, modernizing industry, and improving the lot of the consumer.

35. Individual members of the leadership, either because of particular economic interests or because of special political considerations, or both, have become identified with particular attitudes and programs. Brezhnev, for example, has associated himself most closely with agriculture, defense, and heavy industry. Kosygin, on the other hand, is certainly the most ardent exponent of the need for industrial reform, for which some party and central government bureaucrats have shown little enthusiasm. Politburo member and First Deputy Premier Polyansky, a consistent champion of agriculture, has recently hinted at a major area of contention by assailing as "extremely dangerous" the notions of "some comrades" who believe that last year's successes in agriculture now permit a diversion of resources to other areas of the economy.

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36. While economic issues will continue to occupy a central place in the preoccupations and debates of the leadership, it seems doubtful that they will soon produce another major unsettling of the political scene. There are several factors which may be working to limit the political impact of economic controversy. The economy has recovered from the near-crisis of 1963, and its problems, though still serious, are no longer so acute. Moreover, the leadership appears to have learned from its experiences with Khrushchev that many of the USSR's economic problems are tremendously complex, that official doctrines may obstruct the search for solutions, and that impulse and demagoguery are likely to create additional difficulties. Finally, the increased involvement of institutional elements in the decision-making process, i.e., the growing role of nonparty vested interests, may have the effect of broadening the nature of high-level discussion, widening the circle of those influencing policy, and removing from the debates some of the elements of purely party infighting.

37. Nevertheless, should the round of reform and adjustment which has been going on over the last two years or so fail ultimately to achieve the results hoped for, a renewal of leadership struggle over economic policy is entirely possible. The ambitious aims which Soviet policy pursues externally and the extensive array of unmet needs in the internal society will impose severe strains on available resources for a good many years to come. If economic problems should take on a crisis character again, more radical solutions, carrying implications of change for political institutions as well, might have to be entertained. In such circumstances, the struggles within the party and the competition of power at the top, always present in the Soviet system, could become much more acute than they have been in recent years.

38. The condition of the economy does not at present carry any very marked implications for Soviet external policy. The Soviet leaders appear to be preoccupied with their economic problems, however, and in a general sense they apparently wish to avoid involvements abroad which would bring new economic burdens. Nevertheless, the economy probably does not impose constraints on foreign policy in the sense that the Soviets are foregoing particular initiatives in that field primarily for economic reasons. Ample resources will continue to be available for support of a large arms effort, foreign military and economic aid, and other instruments of foreign policy.

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